

ANNUAL REPORT
OF THE
COMMISSION ON STATE TAX AND FINANCING POLICY



Indiana Legislative Services Agency
200 W. Washington Street, Suite 301
Indianapolis, Indiana 46204

November, 2012

INDIANA LEGISLATIVE COUNCIL

2012

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COMMISSION ON STATE TAX AND FINANCING POLICY

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I. STATUTORY AND LEGISLATIVE COUNCIL DIRECTIVES

The Indiana General Assembly enacted legislation establishing the Commission. The legislation provided the Commission broad authority to study tax and financing policy:

"Sec. 5. (a) The commission shall study and investigate:

- (1) the present state, county, and city tax structure of the state of Indiana;
- (2) its revenue-producing characteristics and effects upon the economy of the state of Indiana;
- (3) its equalities and fairness;
- (4) the enforcement policies and administrative practices related to that tax structure; and
- (5) the costs of collection in relationship to the burden of the tax.

In addition, the Commission shall examine overall administrative matters, fiscal matters, and procedural problems of the various departments of the state, county, and city governments as they relate to tax and financing policy.

(b) The legislative council may refer by resolution any tax or financing problems and correlated matters to the commission for study and research. When any matter is referred to the commission by the legislative council, the commission shall make a study of the problem submitted and shall report the study results in an electronic format under IC 5-14-6 to the legislative council.

(c) The legislative services agency shall provide staff support to the commission." (IC 2-5-3-5)

The Legislative Council assigned the following topics of study to the Commission in the 2012 interim:

- (1) Whether the sales tax exemption for personal property transactions for certain foreign aircraft should apply to all aircraft. (HEA 1325-2012)
- (2) The assessment of outdoor signs. (HEA 1072-2012)
- (3) Whether the value of tax credits under Section 42 of the Internal Revenue Code should be considered in determining the assessed value of affordable housing tax credit property. (HEA 1072-2012)
- (4) Indiana income tax credits. (HEA 1072-2012)
- (5) Financing of solid waste management districts. (SEA 131-2012)
- (6) Developing a comprehensive plan and set of parameters for distressed local units of government and school corporations to borrow funds from the state on an emergency basis. (HR 89-2012)

II. INTRODUCTION AND REASONS FOR STUDY

In addition to the topics assigned by the Legislative Council, the Commission also studied issues related to the following:

- (1) Aviation fuel taxes.
- (2) Innkeeper's taxes.
- (3) Sales taxes.
- (4) Business personal property taxes.
- (5) Medicaid.
- (6) Assessment of farmland.
- (7) Tax collection.
- (8) Public safety answering point (PSAP) funding.
- (9) Marion County assessment ratio study.
- (10) Community revitalization enhancement districts and certified technology parks.
- (11) Tax increment financing for low-density residential redevelopment of brownfields.

III. SUMMARY OF WORK PROGRAM

The Commission met at the State House in Indianapolis on the following dates:

- (1) August 28, 2012.
- (2) September 18, 2012.
- (3) September 24, 2012.
- (4) September 25, 2012.
- (5) October 4, 2012.
- (6) October 17, 2012.
- (7) October 22, 2012.

IV. SUMMARY OF TESTIMONY

The Commission received the following reports from the Legislative Services Agency:

- (1) A Legislative Services Agency memorandum concerning the assessment of outdoor signs (Exhibit H, September 4, 2012).
- (2) A Legislative Services Agency fiscal brief concerning solid waste management districts (Exhibit L, September 4, 2012).
- (3) A Legislative Services Agency Indiana Income Tax Credit Study (Exhibit A, September 24, 2012).
- (4) A Legislative Services Agency fiscal brief concerning community enhancement revitalization districts (Exhibit B, September 25, 2012).
- (5) A Legislative Services Agency fiscal brief concerning certified technology parks (Exhibit C, September 25, 2012).
- (6) A Legislative Services Agency memorandum concerning elimination of personal property assessments and elimination of the 30% valuation floor for personal property (Exhibit J, October 4, 2012).
- (7) A Legislative Services Agency memorandum concerning farmland

productivity factors originally distributed in February, 2012 (Exhibit D, October 22, 2012).

The Commission heard testimony from state agencies, trade associations, advocacy groups, local governments, representatives from higher education, business persons, and interested individuals on the following:

1. Income Tax Credits

The Legislative Services Agency reviewed the usage and effectiveness of eighteen of the state's thirty-eight income tax credits. Economic development officials and interested persons from around the state offered their views of those tax credits.

2. Property Taxes

Seven property tax issues were studied by the Commission:

- (1) Assessment of outdoor signs.
- (2) Funding of solid waste management districts.
- (3) Assessment of business personal property.
- (4) Assessment of Section 42 affordable housing.
- (5) Tax increment financing for low-density residential redevelopment of brownfields.
- (6) Farmland productivity factors.
- (7) Marion County assessment ratio study.

Witnesses in the outdoor advertising business were generally supportive of the valuation schedule implemented under HEA 1072-2012 for property taxes payable from 2012 through 2015.

Representatives of solid waste management districts provided information concerning the existing district revenues and proposed alternative funding sources for the districts: (1) user fees; and (2) a state wide surcharge.

The business community urged the General Assembly to reduce the amount of property taxes imposed upon business personal property. The fiscal impact of eliminating the taxes or eliminating the 30% floor on depreciation was analyzed by the Legislative Services Agency.

The Commission heard differing views on whether the value of a federal income tax credit received under Section 42 of the Internal Revenue Code should be considered when assessing property subject to the tax credit. The Monroe County assessor argued that disregarding the federal income tax credit amounts to an unfair subsidy for properties that often charge rents that are only slightly below market rate. Some developers and financiers of Section 42 housing disagreed with the testimony concerning the rents charged at Section 42 properties, and they

added that higher property taxes would thwart the development of much-needed affordable housing in Indiana. Advocates for affordable housing agreed that increasing property taxes on Section 42 housing would reduce the availability of affordable housing.

The Mayor of Goshen requested legislation to extend tax increment financing to low- density housing in order to provide funding for the remediation of brownfields.

The Commission discussed:

- (1) the history of the use of farmland productivity factors in the assessment of farmland;
- (2) the potential impact on assessments of changes to the federally issued farmland productivity factors; and
- (3) possible methods of mitigating the anticipated impacts on assessments.

The Commission heard concerns about real property assessments in certain neighborhoods in Marion County. The Indiana Department of Local Government Finance (DLGF) reported that it has re-reviewed the county's assessment ratio study and found that it met DLGF standards. It was noted that assessment ratio studies analyze data at the township level. The Commission discussed with the DLGF the possibility of analyzing the data from smaller geographical areas.

3. Sales Taxes

Three sales tax issues were studied by the Commission:

- (1) Taxation of aircraft parts and aviation fuel.
- (2) Sales tax skimming through the use of "zapping" software.
- (3) Taxation of hotel rooms sold through online travel companies.

The aviation industry urged the General Assembly to exempt aircraft parts from the state sales tax regardless of the destination of the repaired aircraft. Witnesses suggested that Indiana would lose repair business to those states that do not impose a sales tax on the parts used in the repair.

The aviation industry also expressed the following concerns with the taxation of aviation fuel in Indiana:

- (1) That Indiana is one of the few states that imposes sales taxes on the sale of aviation fuel.
- (2) That the sales taxes imposed on the sale of aviation fuel are not deposited in a dedicated fund for the support of aviation.
- (3) That aviation fuel taxes are not deposited in a dedicated fund which would leverage more federal grants for the state.

The Commission received testimony on the potential scope of sales tax skimming through

"zapper" software that erases sales from the records of a retail merchant. A potential vendor offered a technological solution that has been used in Quebec and described the impact on sales tax collections that the technology had made in that province.

Witnesses from online travel companies disagreed with Indiana hoteliers and the tourism industry over the appropriate tax base for hotel rooms sold through online travel companies. The Commission heard from both sides on whether the amount charged to the online travel company by the hotel or the amount charged to the consumer (including the online travel company's service charge) represents the appropriate amount on which to calculate the sales tax due on the transaction.

4. Miscellaneous Tax and Fiscal Issues

The Commission studied the following additional issues:

- (1) The Distressed Unit Appeal Board.
- (2) Medicaid fraud.
- (3) Medicaid funding of inmate health care.
- (4) Additional tools needed to collect state and local taxes.
- (5) Public safety answering point (PSAP) funding.

The Office of Management and Budget updated the Commission on the implementation of changes required by HEA 1192-2012 that affect the Distressed Unit Appeal Board. A number of school officials described the impact that the legislation is having on school corporations.

The Office of Medicaid Policy and Planning and the Office of the Attorney General described the agencies' efforts to prevent and detect Medicaid fraud. The agencies reported on the cases prosecuted and the amount of money recovered through administrative, civil, and criminal enforcement actions.

Representatives of the health information technology industry explained that fraud detection is largely occurring after payment is issued to a provider. The witnesses promoted the use of advanced analytics which may enable state agencies to detect fraudulent providers before they are allowed to enter the marketplace and, in other cases, to prevent fraud before payment is issued.

The Indiana Hospital Association urged state government to align the audit procedures of multiple state agencies as closely as possible to ease the burden of compliance placed upon its member hospitals.

The state's Area Agencies on Aging described the effort to educate seniors about Medicaid fraud so that Medicaid recipients may have a role in detecting it.

The possibility that additional inmate health care costs may be paid through Medicaid under the federal Affordable Care Act (ACA) was discussed. The Office of Medicaid Planning and Policy

noted that the additional assistance would be available only if the state opted to expand its Medicaid program under the ACA. The Department of Correction indicated that only a very small percentage of inmates are currently eligible for Medicaid coverage provided to qualified inmates who are treated outside a correctional facility for more than twenty-four hours. A health information technology firm described how advanced analytics could expedite qualifying inmates for the assistance.

The Department of Revenue estimated that as much as \$2 billion is lost annually to noncompliance and that \$300 million to \$500 million of that amount may be recovered by improving compliance. The Department presented a list of proposals for improving its collection and recovery efforts that included adding personnel, improving the Department's technological capabilities, and increasing criminal penalties for tax evasion.

Utah State Senator Curt Bramble presented two options for moving public service answering point funding away from any reliance on the declining number of households using land line telephone service:

- (1) Replacing local fees and taxes with state fees and taxes on various communications services as the State of Virginia has done.¹
- (2) Require electric utilities to collect a state 911 fee on power bills.

Senator Bramble noted that the Virginia approach does not reach the users of various voice over Internet protocol (VOIP) technologies such as Skype, Facetime, or MagicJack. His rationale for using utility bills as a collection vehicle is that most households will continue to use electricity even as the use of VOIP technologies becomes more commonplace.

¹See SEA 345-2012 for a similar consolidation of Indiana telecommunications fees.

WITNESS LIST

Richard Ainsworth, Boston University School of Law
Linda Alexander
Mike Alley, Indiana Department of Revenue
Thom Amdur, National Housing and Rehabilitation Association
Brent Auberry, Faegre Baker Daniels
Brian Bailey, Indiana Department of Local Government Finance
Speros Batistatos, South Shore Convention and Visitors Authority
Brad Baughn, Indiana Department of Environmental Management
Bill Baylor, Emdeon Business Services, LLC
Sen. Curt Bramble, Utah State Senate
Patrick Bennett, National Solid Waste Management Association
Bryce Berg, CGI
Andrew Berger, Association of Indiana Counties
Chad Blacklock, Metropolitan School District of Franklin Township
Garth Brazleton, Indiana Economic Development Corporation
Kevin Brinegar, Indiana State Chamber of Commerce
Ron Breymier, Outdoor Advertising Association of Indiana
Jeffrey Brown, Schahet Hotels
Frank Brummett, Indiana Bankers Association
Brian Budds, Aircraft Owners and Pilots Association
Pat Casanova, Office of Medicaid Policy and Planning
Paul Chase, AARP Indiana
Carter Clarke, LeMar Advertising
Rhonda Cook, Indiana Association of Cities and Towns
Brian Comes, Indianapolis Hyatt
Denny Costerison, Indiana Association of School Business Officials
Larry DeBoer, Purdue University
Patrick Dooley, Fort Wayne-Allen County Airport Authority
Jessica Fraser, Indiana Institute for Working Families
Andy Frazier, Indiana Association for Community Economic Development
Bart Giesler, John Frick & Associates
Kelli Garvanian, Emdeon Business Services, LLC
Terry Guerin, National Solid Waste Management Association
Matt Hagans, Eagle Creek Aviation
Katrina Hall, Indiana Farm Bureau
Greg Henderson, SAS Institute
Heath Holloway, Legislative Services Agency
David Holt, Conexus
Martin Ingram, Muncie Aviation
Cris Johnston, Indiana Office of Management and Budget
Ann Kaiser, Indiana Office of Management and Budget
Mayor Allan Kauffman, City of Goshen
Frank Kelly

Sen. Luke Kenley
Justin Kintz, Orbitz Worldwide
Jeff Kittle, Herman and Kittle Properties, Inc.
Gina Kostoff, Fort Wayne Urban Enterprise Association
John Krauss, Indiana University Public Policy Institute
Bob Kuzman, Kopka, Pinkus, Dolin, & Eads
Kristen LaEace, Indiana Association of Area Agencies on Aging
Jim Landers, Legislative Services Agency
Sen. Jean Leising
Amy Levander, Krieg DeVault
Nate Lichti, Hamilton County Area Neighborhood Development, Inc.
John Livengood, Indiana Hotel and Lodging Association
Andy Miller, Bose Public Affairs Group
David Miller, Office of the Attorney General
Kristina Morehead, Office of Medicaid Policy and Planning
Lucinda Nord, Indiana Association of United Ways
Matthew O'Connor
Michael O'Connor, Eli Lilly and Company
Sean O'Connor
Bruce Palin, Indiana Department of Environmental Management
Robert Plantenga, Tippecanoe County Treasurer
Chad Pittman, Indiana Economic Development Corporation
Allen Pope, Office of the Attorney General
Paul Powell, Hawker Beechcraft
Diane Powers, Legislative Services Agency
Andrew Pritchard, Department of Corrections
Phil Ray, Indianapolis Marriott
Jason Regger, Cook Medical, Inc.
Julie Rhodes, Association of Indiana Solid Waste Management Districts
Bill Riggs, Mt. Vernon Community School Corporation
Doug Risser, Menno Travel Service
Steve Sacksteder, Four Rivers Resource Services
Sen. Scott Schneider
David Schwab, Indiana Department of Local Government Finance
Judy Sharp, Monroe County Assessor
Eric Shields, Indiana Economic Development Corporation
Bob Sigalow, Legislative Services Agency
Jason Sipe, Indiana Housing and Community Development Authority
Jamie Shepherd, Howard County Assessor
David Sklar, Indiana Coalition for Human Services
Aaron Smith, Watchdog Indiana
Rep. Ed Soliday
Andrew Swain, Office of the Attorney General
Richard Sprague
Mark St. John, St. John & Associates

Brian Tabor, Indiana Hospital Association
Rep. Jeff Thompson
Jim Tidd, Miami County Economic Development Authority
Colin Tooze, Expedia, Inc.
John Urbahns, City of Fort Wayne
Connie Vickery, Indiana Restaurant Association
Sen. Greg Walker
James Wallace, Indiana Association of Convention and Visitors Bureaus
Bill Waltz, Indiana State Chamber of Commerce
Rick Wajda, Indiana Builders Association
Jeff Whiting, City Real Estate Advisers
Mark Wuellner, Indiana Housing and Community Development Authority